Public Accounts: Other Issues

1) The AG has supporting advice and opinions

The AG obtained supporting advice from current Auditors General in Canada, and the federal AG, external advisors, including the recently retired Director of the Canadian Public Sector Accounting Board, who all agree that rate regulated accounting is not permitted under Public Sector Accounting Standards.

The AG has also received accounting opinions/white papers/memos from other smaller accounting firms that generally support her position.

IESO's position:

- The IESO regularly reviews its accounting policies to ensure that they provide transparent and relevant financial reporting that most accurately represents the IESO's assets and liabilities and meets the needs of its financial statement users.

- The IESO's auditor, KPMG and one other big-four accounting firm agree that as PSAS is silent on rate-regulated operations, US GAAP is an appropriate accounting framework to look to for guidance on rate-regulated operations. Furthermore, the accounting firms agree that regulatory accounting under ASC 980 is not an exemption from the application of US GAAP.

- The IESO implemented regulatory accounting after thorough review and consideration by senior management and Board, engagement with our external auditor and consultation with the Provincial Controller's Office.

Note: The International Financial Reporting Standards (IFRS) Foundation has had initial discussions about whether its standards should be amended to reflect the effect of rate regulation. In its initial discussion, it has tentatively decided that: "the present regulatory right—to charge a rate increased by an amount that as a result of past events—meets the definition of an asset in the *Conceptual Framework*. All 14 Board members agreed with this decision."

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2) The AG claims the IESO was uncooperative with the OAGO's attest audit. The IESO refuses to sign the AG's management representation letters and audit planning report and have not provided written responses to the standard fraud questions.

The OAGO made several requests for the IESO Board to sign a management representation letter and audit planning report. The Board agreed to cooperate with the AG's audit, but will not sign the letter, or the planning report, which could be perceived as uncooperative and/or obstructionist. The IESO responded verbally to the fraud questions.

IESO's position:

Audit cooperation

- The IESO has made every effort to be forthright and fully responsive to the OAGO's requests for information.

- The IESO recognizes the Auditor General's statutory role and authority to perform an audit of the IESO and cooperated fully with the OAGO in the completion of the special audit undertaken.

- In recognition of the OAGO's work, the IESO instructed its auditor, KPMG to deliver their audit report to the AG and make available their working papers in respect of the AG's audit. The IESO also provided copies of any materials provided to KPMG in respect of their audit and offered OAGO staff free access to all books, accounts, financial records, reports, files and all other papers, things or property belonging to or used by the IESO – including a copy of the management representation letter provided to KPMG.

- The IESO likewise instructed its audit partner to cooperate and share relevant information with the OAGO's staff.

- ~~The IESO has made every effort to be forthright and fully responsive to the OAGO's requests for information.~~

- The IESO cooperated with the Office of the Auditor General to provide information, including the 2017 financial statements prepared by management, and for access to management for assistance in understanding such information.

- Throughout the OAGO's audit:
    - Accommodations were made to extend the duration of OAGO staff on IESO premises from the initial two weeks requested, to seven weeks.

- During this time, the IESO received ~~over~~ 200 information requests from OAGO staff. The IESO will respond to all outstanding requests ~~will be provided~~ before the audit concludes.
- IESO accommodated every meeting request; ~~over 35~~about 40 meetings took place between IESO and OAGO staff.
- We accommodated all the AG's requests to meet with our Board and Audit Committee.
- Throughout their audit, OAGO staff were located on IESO premises and had direct access to IESO staff.

Management representation letter and audit planning report

- Referring the Auditor General's Act, it says that [IESO] has to provide the AG with the requested information – which we have - ~~;~~ it does not compel IESO to provide or accept a management representation letter and/or planning report.

- As communicated to the AG, at the time of her request, the IESO had already retained KPMG as its auditor – and therefore declined to sign a second management representation letter.

- As the IESO did not formally engage the AG to conduct its audit for the year-ending December 2017, therefore, ~~the IESO~~ our Board was not in a position ~~did not deem it necessary to~~ sign the AG's audit planning report.

Note: One key component of planning report is that the IESO agrees to rectify any identified audit concerns; which will not be true for the regulatory issue as it concerns AG.

Standard fraud questions

- Fraud questions were responded to verbally on February 2, 2018 by the IESO's Board Audit Committee Chair.

Note: It's unclear whether the IESO intends to provide a written response to the fraud questions.

3) The AG asserts the accounting change was led by government's desire to keep costs associated with the Fair Hydro Plan off the province's consolidated financial statement, discrediting the IESO Board's governance and independence.

The AG's *Special Report* notes that the changes in accounting policy at IESO were found to be a "deviation from Canadian PSAS in favour of U.S accounting to try to satisfy the Province's objective for the Policy Decision to have no bottom-line impact on its annual results and no impact on debt".

On a call between Audit Committee and the AG, the AC Chair stated that the accounting decision was made by Board independent of government and that it would be disheartening to see it reported as a political decision. The AG noted that in looking into the issue, she had access to IESO emails with Treasury and Ministry and knows that a conscious decision to have regulatory assets on statements was fundamental the Fair Hydro Plan.

Note: It's unclear whether the AG believes the Board was aware of the link to Fair Hydro Plan, or if she is claiming that management was aware and did not inform the Board.

IESO's position:

- The IESO is a government agency and works regularly with government on the development and implementation of various government policies affecting Ontario's electricity sector - the Fair Hydro Plan is no different.
- Throughout considerations to change accounting practices, the IESO engaged the Ministry, the Treasury Board Secretariat and its external auditors to ensure that any change would be applicable with current and future government policy.
- However, it's important to note that the IESO considered the accounting policy changes on their own merits, and found that the changes would offer the IESO greater transparency into the market accounts it oversees and better financial reporting of its regulated assets.
- The IESO sought a white paper prepared by KPMG that found the accounting changes were permitted in PSAS and would be able to accommodate contemplated policy.
- The IESO adopted the accounting changes on March 15, 2017 after discussions with KPMG and the IESO Board.
- However, had the Fair Hydro Plan never come into effect, the IESO would still maintain these changes.

4) The AG has raised the competency, qualifications and decision-making of the IESO's Board.

IESO position:

- The IESO's Board of Directors possesses a wealth of skills and diverse sector experience in energy, agriculture, regulation, healthcare, environment, transportation, information technology and Indigenous affairs.

- The IESO Board's expertise spans to: public, private and non-profit sectors, finance and accounting, economics, human resources, strategic planning, procurement, legal, risk management, financing, capital markets, engagement, marketing and branding and program design and implementation

Notes: ~~Internal Audit's Entity Control Review makes reference to regular Board evaluations and skills assessment, John Rattray to provide results.~~

From the Entity Control Review, item 12: *"Without complete reporting to the BoD, there is a risk that BoD members do not have the required information to execute their governance responsibilities efficiently and effectively."*

5) The AG stated that the IESO could have saved the cost of KPMG's audit by allowing her office to conduct the audit instead, free of charge.

IESO's position:

- At the time the Auditor General made this offer, the IESO had already engaged KPMG as its auditor.

- The IESO recognizes the Auditor General's statutory role and authority to perform an audit of the IESO and has fully cooperated ~~The IESO welcomed the OAGO staff and fully cooperated~~ in providing the information and context requested to assist with the attest audit.

If pressed on amount spent on KPMG 2017 audit:

- The IESO spent $65K on the KPMG's auditing services, which I think you will find is in line with other organizations of our size.

- ~~The amount of time and resources that were spent by the IESO, responding to the OAGO's audit requests that went well beyond the scope of a standard financial audit were not insignificant.~~

6) AG Audit Finding: Accounts Payable Clearing Account

The OAGO has found an unreconciled balance of $8 million in the accounts payable clearing account. The amount was related to amounts paid to CF&R, the organization previously responsible for Save on Energy's coupon program.

IESO's position:

- The IESO recently received the AG's special audit findings and will review and discuss each finding and recommendation closely before responding.

Note: This was also a finding of KPMG's 2016 audit. At that time, the IESO gave them an explanation on this account that was incorrect. This was not resolved at the invoice level and appropriate entries were not made until the 2017 audit was underway. A draft management response indicates that the IESO agrees this needs to be resolved and commites to putting processes in place to prevent this from reoccurring and will report back to the Audit Committee upon resolution.

7) AG Audit Finding: Unreconciled Security Deposits

The IESO has not reconciled security deposits for a number of years and have not yet determined to whom $1.5 million may be payable to in the future.

IESO's position:

- The IESO recently received the AG's special audit findings and will review and discuss each finding and recommendation closely before responding.

Note: These are deposits tied to applications that did not lead to a contract, and for which the proponents have not applied for a return of the deposit. Draft management response indicated that management agrees better record keeping is required and has committed to further investigate the issue.

8) AG Audit Finding: HR Pay Progressions

Of a sampling of pay progressions (promotions) 30% were found to have not followed the appropriate workflow process.

IESO's position:

- The IESO recently received the AG's special audit findings and will review and discuss each finding and recommendation closely before responding.

Notes: The IESO introduced a new Human Resource Information System (HRIS) in 2016 to automate some of its HR processes. This tool has some ability to facilitate a workflow and controls for processing pay progressions, but cannot accommodate all requirements of the collective agreements. This issue was previously identified and is being addressed through a tool enhancement, scheduled for Q3 2018. It will also be factored into the new payroll system design.